

BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of        )  
GARRETT FREIGHTLINES, INC.        )

Appearances:

For Appellant:     Otto H. Tschanz, Jr., Treasurer-  
Comptroller; S. W. Erickson,  
Certified Public Accountant

For Respondent:    Burl D. Lack, Chief Counsel;  
A. Ben Jacobson, Associate Tax  
Counsel

O P I N I O N

This appeal is made pursuant to Section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the protest of Garrett Freightlines, Inc., to a proposed assessment of additional franchise tax in the amount of \$1,381.36 for the income year 1954. Of this amount only \$192.45 is in dispute,

Appellant is an Idaho corporation with headquarters at Pocatello, Idaho. It is engaged in the motor freight business in California and other states. Its business and rates are regulated by the Interstate Commerce Commission. For the purpose of determining rates the Commission requires Appellant to use the straight-line method for computing depreciation. For all income periods prior to the year 1954 Appellant also computed depreciation for Federal and State tax purposes by the straight-line method. For the income year 1954 it changed to the sum-of-the-digits method to compute depreciation on new trucks, trailers and auto equipment for tax purposes. The amount of depreciation so computed by Appellant was \$43,642.57. The Franchise Tax Board recomputed the depreciation by the straight-line method and determined the allowable amount to be \$14,070.91. The right of Appellant to use the sum-of-the-digits method is the only issue raised by its appeal.

The sum-of-the-digits method of computing depreciation for certain property acquired or constructed after December 31, 1953, was authorized for Federal tax purposes by Section 167(b) of the Internal Revenue Code of 1954. The change to

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that method by Appellant has been approved by the Internal Revenue Service. It is the contention of Appellant that the language of Section 24121g of the Revenue and Taxation Code (now Section 24349) and Bank and Corporation Tax Regulation 24121g(5) is sufficiently broad to permit the use of this method in the computation of its State tax. During the year in question Section 24121g of the Code provided for the deduction of a reasonable allowance for exhaustion, wear and tear and obsolescence of property used in a trade or business. Regulation 24121g(5) provided, in part, that the capital sum to be recovered by depreciation should be charged off over the useful life of the property, either in equal annual installments or in accordance with any other recognized trade practice.

At its 1955 session the California Legislature extensively amended those parts of the Revenue and Taxation Code comprising the Bank and Corporation Tax Law and the Personal Income Tax Law to conform those laws with the 1954 revision of the Internal Revenue Code. Amendments drafted by the Franchise Tax Board to conform the depreciation provisions of the statute with Section 167(b) of the Federal Code, however, were rejected in committee. Similar amendments were introduced and rejected at both the 1956 and 1957 sessions of the Legislature.

Prior to the 1954 revision of the Internal Revenue Code the sum-of-the-digits method of computing depreciation was relatively unknown and its use was not authorized for either Federal or State tax purposes. Section 167(b) of the Federal Code now permits its use only with respect to specified property acquired or constructed after December 31, 1953. As contrasted to the straight-line method of computing depreciation, the sum-of-the-digits method allows a much greater depreciation during the early years of the anticipated life of the property,

Methods of computing depreciation are methods of accounting and a change in the method of accounting may be made only with the advance consent of the Franchise Tax Board as prescribed in Bank and Corporation Tax Regulation 25201b(1). (See I.T. 3818, C.B. 1946-2, 42 and Rev. Rul 57-352, I.R.B. 1957-31, 9). Since the record does not affirmatively show that Appellant complied with the requirements of that regulation it would appear that the Franchise Tax Board was fully justified in refusing to retroactively approve the change in method. In addition, Appellant continued to use the straight-line method of depreciation for purposes of fixing rates, and has not demonstrated by competent evidence that the accelerated depreciation computed by the sum-of-the-digits method for tax purposes was reasonable, or that its

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use properly reflected the income of Appellant for the year in question; And finally, we are of the opinion that until such time as the Legislature specifically authorizes the deduction of accelerated depreciation computed by the ~~sum-of-the-digits~~ method, as Congress has done with respect to Federal taxes, the determination by the Franchise Tax Board that this method is not acceptable for computing depreciation is within the discretion vested in that Board,

O R D E R

Pursuant to the views expressed in the Opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to Section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the protest of Garrett Freightlines, Inc., to a proposed assessment of additional franchise tax in the amount of \$1,381.36 for the income year 1954 be and the same is hereby sustained,

Done at Sacramento, California, this 2nd day of October, 1957, by the State Board of Equalization.

Robert E. McDavid, Chairman

Paul R. Leake, Member

J. H. Quinn, Member

George R. Reilly, Member

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ATTEST: Dixwell L. Pierce, Secretary